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For the attention of Ade Balogun

6 August 2009

Dear Sirs

Consultation on draft guidance for how to measure and report your greenhouse gas emissions

We appreciate the opportunity to comment on the draft guidance on how to measure and report your greenhouse gas ("GHG") emissions.

In general we believe the guidance is helpful to companies in reporting their greenhouse gas emissions. Basing the guidance on the internationally accepted GHG Protocol is an important step, but to facilitate greater comparability between companies, reducing some of the options available under the GHG Protocol is desirable.

Our detailed comments are set out in the Appendix to this letter. Our intention in making these recommendations is to help develop a GHG reporting standard that is of value to business and practical to implement. We would pick out six particular points as important:

1 Decide which companies will be required to report in 2012

The current timetable proposes that any mandatory reporting will be introduced only in 2012. We believe that it is important that government decides much earlier to which companies mandatory reporting will apply. We believe any mandatory reporting should apply initially to larger entities although recognise smaller entities should be encouraged to consider voluntary reporting. It should not be underestimated how much effort and time is required to put in place appropriate processes, systems and controls for gathering the required information, particularly for entities which are complex or have many overseas locations. Without clarity, some companies may be too late in starting while others may waste effort if they are eventually not required to report.

2 Set a clear GHG emissions Reporting Standard, supported by separate guidance to help companies with implementation

To provide companies with clarity on what they need to report, the guidance needs to be converted into a reporting standard. This standard could be supported by a guidance document to help different companies report in accordance with the standard.

3 Best practice versus standard practice

We understand the desire to differentiate the 'minimum' level of reporting which would constitute Standard Practice, but generally believe the recommendations that go beyond Standard Practice should be labelled differently – possibly as "optional practice". While extending reports to include these additional options would represent "better practice", we believe that it is unlikely that this level of reporting will constitute "best practice". In any event it would not be appropriate for Defra to define or restrict best practice at this stage.

4 Create separate standards for large companies and SMEs

Defra could create one reporting standard for large companies and a lighter version for SMEs. This would enable more tailoring of requirements to suit the size of company and ensure the documents remain relevant and focused.

5 Recommend the reporting includes management commentary on broader climate change risks, strategies and performance

Reporting on climate change risks, strategies and performance in the form of a commentary will help companies better understand and demonstrate how climate change impacts their business and the actions they should take. This understanding should help companies (and investors) appreciate why monitoring and reporting GHG emissions is of benefit to the business rather than simply constituting more burdensome regulation.

6 Provide further guidance on the use of estimates and assumptions

The accuracy and relevance of companies GHG emissions reporting is undermined if there is a high degree of assumptions, extrapolations, estimates and even 'guestimates' rather than appropriate measurement. Defra should provide guidance on what constitutes an appropriate level and type of estimate and assumption to ensure meaningful and accurate reporting.

We encourage government to use the development of this GHG reporting requirement in the UK to lead and influence the development of international standards. It is important to avoid the introduction of widely different requirements by authorities in different parts of the world which could put an unwelcome burden on multinational companies. Developing a consistent approach could also enable suppliers to more easily comply with GHG emissions/reporting that is beginning to be required by large customers, often based overseas.

We would be happy to discuss our views with you and if you have any questions in connection with this letter, please contact Alan McGill on 0207 212 4348 or Paul Rew on 0207 804 4071.

Yours faithfully

Pricewaterhousecoopers LLP

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Consultation on draft guidance for how to measure and report your greenhouse gas emissions

Appendix

Q1. Does the guidance provide enough detail? Are there any issues on which you would welcome further guidance?

Decide which companies will be required to report in 2012

The current timetable proposes that mandatory reporting, if introduced, will only apply in 2012. We believe that it is important that government decides much earlier to which companies mandatory reporting will apply. It should not be underestimated how much effort and time is required to put in place appropriate processes, systems and controls for gathering the required information, particularly for entities which are complex or have many overseas locations. Without clarity, some companies may be too late in starting while others may waste effort if they are eventually not required to report.

Level of guidance provided

The level of guidance provided throughout the document varies. In some places in-depth guidance is included, for example on choosing the organisational boundary and dealing with leases. However other areas are light on guidance, for instance guidance on outsourcing and bio-sequestered carbon.

Part 6 focuses on the collection of activity data. This section would benefit from an overview of what constitutes good characteristics of activity data.

Scope 3 emissions

Scope 3 emissions are an area with which most businesses are currently struggling and the concept of reporting only on significant emissions is a useful principle to introduce.

It is worth noting that there is currently work in progress on the GHG Protocol to provide further guidance on scope 3 reporting for both corporates and products. Defra's guidance should aim to align with developments in the GHG Protocol to avoid future conflicts.

Emission factors

More guidance is required on appropriate sources of overseas emission factors. We support the notion that overseas emissions should not use Defra/DECC factors unless appropriate alternatives are not available. But where appropriate alternatives are available the guidance could highlight approved overseas factors for reporting in accordance with the Defra standard. (see question 2 Recommendation 5 below)

Information quality and estimations

As companies begin to monitor and report GHG emissions data they may find it hard to collect actual activity/emissions data and therefore need to make assumptions and estimates to complete the reporting in accordance with the Defra guidance. However, there comes a point where estimates and assumptions become so significant as to undermine the relevance of the reported data.

Defra should consider setting a threshold for the amount of estimation and assumption allowed to report in accordance with the standard. Guidance should be developed on the difference between an appropriate estimate/assumption and what constitutes an inappropriate 'guestimate'.

Q2. Do you agree with all the recommendations? It would be helpful if you could comment on any recommendations with which you disagree.

Recommendation 1: Organisational boundary

One of the key problems with using the GHG Protocol is the amount of choice it provides and the resultant lack of comparability between companies. Stakeholders are often interested in comparing the emissions from different companies and the Defra standard should aim to facilitate this.

The organisational boundary is an area where applying different approaches can produce significantly different reported emissions. We support that the guidance recommends an approach to increase comparability based on the financial control concept, particularly for companies that are new to reporting. We suggest the recommendation should be expanded for companies that have already chosen an alternative approach requiring them to explain the reasons for choosing an alternative and the significant differences that arise compared with applying the financial control approach.

Recommendation 2: Measure or calculate total emissions on a global basis

We agree.

Recommendation 3: Operational boundary

We agree that minimum reporting should cover both scope 1 and scope 2 emissions.

Scope 3 emissions are more relevant for some industries than others. For instance, scope 3 emissions for a power generation company are relatively insignificant, whereas they are the majority of emissions for a final product assembly company. Therefore it is worth considering basing requirements for reporting scope 3 emissions on the level of contribution to total emissions, or setting a materiality threshold for the required inclusion of scope 3 emissions.

Recommendation 4: Greenhouse gases for inclusion

We agree that reporting should focus on the six Kyoto GHGs. However companies should be allowed to exclude specific Kyoto gases if in total they are determined to be immaterial to their total GHG emissions. This will save companies from implementing costly systems and processes to collect information that is not business critical.

Few companies are likely to emit significant non-Kyoto GHGs. Therefore it will only be best practice for a small number of companies. We suggest that this is not labelled as best practice, but rather noted as relevant for certain industries.

Recommendation 5: Emission factors

It is not clear whether the recommendation of applying the Defra/DECC emission factors for the UK should be applied to all global emissions or just emissions from the UK. We would recommend using a hierarchy for selecting emission factors.

Tier 1 (best) – Customised emission factors reflecting the emissions from the actual source (e.g. on-site stationary combustion or process emissions).

Tier 2 – Local country emission factors (e.g. Defra/DECC factors for UK emissions) or industry factors for process emissions or other well recognised international sources such as WRI.

Tier 3 – In the absence of local country emission factors, default to Defra/DECC factors.

Recommendation 6: Report total gross GHG emission

We agree.

Recommendation 7: Optional reporting of net CO_2e emissions

The principle of reporting separately purchased emission reductions and a net CO_2e emissions figure is supported. Please see comments below on Defra's proposed emission reduction criteria.

Recommendation 8: Report on total scopes 1 and 2 emissions using an intensity ratio

We agree.

Recommendation 9: Emission reduction targets

A Reporting Standard is not the place to mandate the setting of targets. A supporting guidance document could include a discussion on the merits of setting an emission reduction target.

Q3. Do you agree with the criteria given to determine which scope 3 emissions are significant? If you disagree, please suggest additional or alternative criteria.

Reporting scope 3 emissions is challenging and the provision of guidance on what constitutes significant scope 3 emissions will help companies report meaningful emissions without feeling the need to report a complete set of scope 3 emissions.

With regard to the Step 3 set of criteria outlined on page 55, we view the criteria 'scale', 'importance to your business' and 'stakeholders' as the most important. 'Potential for reductions' and 'ability to influence data gathering' are likely to cause conflicts with the other criteria and potentially lead to significant scope 3 emissions not being reported.

The guidance could benefit from more prescription, for example any source/activity that is deemed material to total scope 1, 2 and 3 emissions should be reported. It is recognised that this will require a company to have a high level understanding of the scale of emissions from its entire value chain, but reporting on 'significant scope 3 emissions' without this will prove challenging. The reporting should include a narrative description of known sources of scope 3 emissions which are not currently measured.

Q4. Your comments are sought on the emissions data that we recommend you report?

We believe that the recommendation on reporting should be restructured to identify (1) what should be reported and (2) where it should be reported.

The recommendation on <u>what</u> should be reported should include:

(a) the data proposed in the guidance in the form of a "primary statement"

(b) the explanation of the reporting policy choices adopted by the company, to allow a reader to understand the composition of the data.

(c) supporting notes as deemed appropriate by the company to analyse the data further.

(d) a management commentary to explain the company's emissions "performance" for the period covered, the approach to climate change risk, emissions reduction, target setting and management/governance.

Please refer to our example GHG emissions Report for a fictional company – Typico plc (www.**pwc**.co.uk/pdf/carbon_reporting_may_09.pdf).

As to where the report should be made available, we believe that the full report should be included on the company's website and, in most cases, only a summary should be included in the company's business review in its annual report.

Q5. What is your view on the supporting explanations that it is suggested organisations should include in their report?

As noted above, we believe the supporting information included in our GHG emissions reporting example, Typico plc, is the most sensible format. This splits supporting explanations into a primary GHG emissions statement and three other areas: reporting policies, notes to the primary statement and management commentary.

Reporting policies

The 'reporting policies' element of the supporting explanations is essential to gain a full understanding of the reported emissions and should be mandatory rather than only recommended. Any company that wants to report in accordance with Defra requirements will need to develop their own reporting policies, so the reporting of those policies as mandatory should not be onerous.

Notes

Companies with significant international operations and different business segments should report segmental analysis as standard. A breakdown of emissions by source will provide users with a better understanding of activities in the business that drive GHG emissions and should also be included as standard reporting.

The note on acquisitions and divestments should be included for companies that have gone through significant business changes in a year. This note also takes account of changing baselines and targets as a result of acquisitions and divestments.

Management commentary

A management commentary section could include explanations such as the reasons for year on year movements and the governance arrangements pertaining to GHG emissions reporting and management. The extent of the commentary will vary depending upon the size and circumstances of the company.

Q6. Your comments are sought on the external emission reductions activities that we have identified as 'good quality' criteria that these reductions activities should meet.
Green tariffs Disallowing domestic emission reduction projects could result in reduced demand for green electricity tariffs. Removing this incentive for energy companies is likely to have a detrimental affect on the achievement of a low carbon UK infrastructure. This standpoint needs further consideration by the energy companies and companies currently sourcing green electricity.
Q7. Your comments are sought on how organisations should account for the renewable electricity that they generate.
Including emissions electricity generation from zero carbon sources at grid average factors is not representative of the actual emissions produced and therefore does not seem logical in our view. Mandating that companies use a grid factor in reporting gross emissions could turn companies away from zero/low carbon energy investments as they may feel unrewarded for this when reporting in accordance with Defra guidance. The Defra GHG emission reporting guidelines should drive support for onsite zero / low carbon energy.
Q8. We welcome your comments on the attached impact assessment for this policy? Do you have any estimates for how long it would take you to follow the guidance?
The costs involved in GHG emissions monitoring and reporting will vary substantially depending on the size of company, business structure, international reach, and existing level of knowledge. The estimates provided in the Impact Assessment appear to be very low. It is likely to take companies more time than estimated to understand the implications of the guidance and develop reporting systems, processes and controls to meet the requirements. Even for companies currently reporting GHG emissions this is likely to take a significant length of time and investment in system/process changes. For companies reporting for the first time, significant time will be involved in sourcing activity data in the right format, embedding behaviours to collect the data, developing governance processes to oversee external reporting and providing appropriate training. We believe the Average Annual Cost of voluntary reporting is likely to be significantly higher than the total of £7m for all companies. First year one-off set up costs are likely to be significantly more than the Average Annual Costs.
Q9. Please provide any general comments on the guidance, especially any issues where you would welcome further explanation.
Split the document into a reporting standard and supporting guidance on implementing the standard Splitting the guidance into two parts; the first setting out the reporting standard which only includes the rules that need to be applied to report in accordance with the Defra GHG emissions requirements; and the second section incorporating further guidance to help companies apply the reporting standard would have two benefits.

Firstly, should the decision be taken to make the reporting mandatory in 2012, splitting the document into these two parts would facilitate identifying exactly what is mandatory. Secondly, it would enable the guidance to be more tailored to different types and sizes of company, for instance there could be separate guidance for first time reporters and experienced reporters, or carbon intensive and lower carbon sectors. The guidance could be enhanced and added to without changing the standard.

Best practice versus standard practice

We understand the desire to differentiate the ‘minimum’ level of reporting which would constitute Standard Practice, but generally believe the recommendations that go beyond Standard Practice should be labelled differently – possibly as “optional practice”. While extending reports to include these additional options would represent “better” practice, we believe that it is unlikely that this level of reporting will constitute “best practice”. In any event it would not be appropriate for Defra to define or restrict best practice at this stage.

Create separate standards for large companies and SMEs

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